

Introduction to Money

What IS money?

- Anything generally accepted as a medium of exchange



What makes an item “money?”

AKA – Characteristics of Money

- **Durability:** can be used without significant damage
- **Portability:** can be carried from one place to another in varying degrees
- **Divisibility:** can be divided into smaller units
- **Stability:** will keep its value over time
- **Acceptability:** must be accepted in the area



3 Basic FUNCTIONS of MONEY

- **1. Provide a medium of exchange**
 - - must be accepted by a large majority of sellers in a community
 - **2. Serve as a standard of value (Unit of Account)**
 - - must be able to measure relative value of goods
 - - Good X can be quoted in a “price” that everyone understands
 - - can help to explain opportunity costs in specific terms
 - - provides a way to compare profits and losses
 - **3. Store its value**
 - - must be able to save (store) and use it later at the same face value (not same REAL value)
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What makes money valuable?

- **Commodity money:** an item that is naturally valuable and desirable just because of what it is
 - gold, silver, rubies, gems, diamonds
 - historically things such as salt, tobacco, elephant hair, and whale's teeth have been used
- **Representative money:** an item that has value because it "represents" something with value
 - Representative money has no value of its own
 - a piece of paper that represents a stack of gold would be an example
 - you could get a bill of credit (piece of paper from the treasury) that represented a certain amount of SPECIE (gold or silver) and pay your debts with that
- **Fiat money:** an item that is valuable because of a government decree
 - - US money is this way

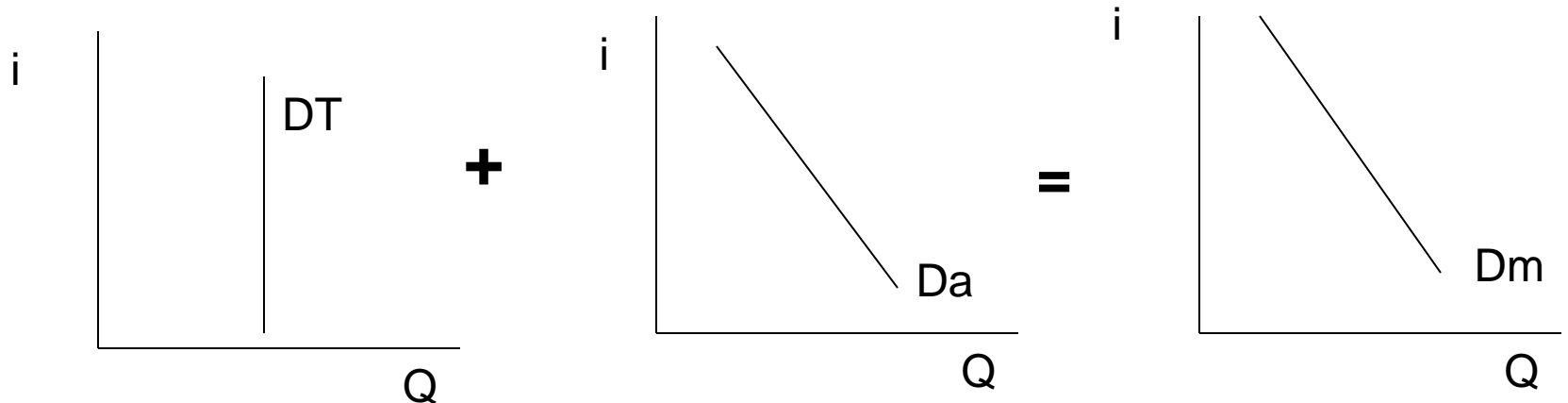
What is the MONEY SUPPLY

■ 4 “TYPES” of Money

- ❑ M0 – Purely cash
- ❑ M1 – Transaction money
 - M0 + checkable deposits
 - FED tracks this day to day (typically in the \$1.5billion range)
- ❑ M2 – Broad Money
 - Everything in M1 + “time deposits”= savings accounts, money market accounts, and other less liquid accounts (near money)
- ❑ M3 – “All” Money
 - Everything in M2 + very large time deposits and repurchase agreements between corporations and/or government agencies

Money Market

- Supply of money set by FED
- Demand for money determined by adding:
 - Demand for transactions (fairly inelastic)
 - Demand of assets (elastic relating to interest rates)



Money Market

- Measure of M1 in the economy

